

Office of Chief Counsel  
Internal Revenue Service

**memorandum**

CC:MSR:KSM:KCY:TL-N-471-99  
DPKensinger

date: **JAN 29 1999**

to: Director, Kansas City Service Center  
P.O. Box 7905, Stop 4100, RA Unit, Annex 2  
Shawnee Mission, Kansas 66207  
Attn: Bridgette E. Dunmore

from: Assistant District Counsel, Kansas-Missouri District, Kansas City

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subject: Application of Sequa Corporation Decision

[REDACTED]  
Advisory Opinion - Significant

This refers to your request for advice with respect to the application of the decision in Sequa Corporation v. United States, 97-1 U.S.T.C. ¶ 50,317 (S.D.N.Y. 1996) to the payment of interest to the above-named taxpayer. Earlier we had provided you with a partial response but were unable to provide a complete response. We have now obtained additional information as well as the advice of the National Office on this situation. Consequently we can now give you a complete response.

DISCLOSURE STATEMENT

This advice constitutes return information subject to I.R.C. § 6103. This advice contains confidential information subject to attorney-client and deliberative process privileges and if prepared in contemplation of litigation, subject to the attorney work product privilege. Accordingly, the Examination or Appeals recipient of this document may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure. In no event may this document be provided to Examination, Appeals, or other persons beyond those specifically indicated in this statement. This advice may not be disclosed to taxpayers or their representatives.

SIGNIFICANT

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This advice is not binding on Examination or Appeals and is not a final case determination. Such advice is advisory and does not resolve Service position on an issue or provide the basis for closing a case. The determination of the Service in the case is to be made through the exercise of the independent judgment of the office with jurisdiction over the case.

We will not repeat the facts from our prior memorandum dated September 18, 1998 but only summarize them briefly here. The taxpayer filed its income tax return for the period ended June 30, [REDACTED] on [REDACTED]; this return showed an overpayment in the total amount of \$ [REDACTED]. The overpayment was applied to the next fiscal year (the period ended June 30, [REDACTED]). The taxpayer, however, made estimated tax payments for the year ended June 30, [REDACTED], which fully paid the liability for that year.

Subsequently, the Service assessed a deficiency in the amount of \$ [REDACTED] on [REDACTED] the taxpayer paid this deficiency by an advance payment on [REDACTED]. The general issue is when interest begins to run on this deficiency. When we issued our earlier opinion we did not know the tax period to which this taxpayer actually applied the overpayment from fiscal [REDACTED]; nor did we know the position our National Office would take with respect to the application of Sequa to this situation.

The transcripts for the taxpayer's taxable years ended June 30, [REDACTED], [REDACTED], [REDACTED], [REDACTED], [REDACTED] and [REDACTED] show that the overpayment credits for fiscal [REDACTED] ([REDACTED]) were not used to pay estimated taxes for the tax years ended June 30, [REDACTED] and [REDACTED] ([REDACTED] and [REDACTED]). The estimated payments for fiscal [REDACTED] ([REDACTED]) were less than the total tax liability and, according to the transcript of account, a portion of the overpayment credit from fiscal [REDACTED] ([REDACTED]) was used to pay the tax for fiscal [REDACTED] ([REDACTED]) with a resulting overpayment of \$ [REDACTED] for fiscal [REDACTED]. That overpayment was applied to the estimated taxes for fiscal [REDACTED] ([REDACTED]). The estimated taxes for fiscal [REDACTED] were full paid and there was an overpayment from fiscal [REDACTED] which was applied to fiscal [REDACTED] ([REDACTED]). A portion of the overpayment credit from fiscal [REDACTED] ([REDACTED]) was used to satisfy the tax liability for fiscal [REDACTED] ([REDACTED]). There was an overpayment for fiscal [REDACTED] which was credited fiscal [REDACTED] ([REDACTED]). Thus, it appears that none of the overpayment from fiscal [REDACTED] ([REDACTED]) was needed to satisfy the estimated taxes for fiscal [REDACTED] ([REDACTED]), and that such overpayment credits were not used until the fiscal [REDACTED] ([REDACTED]) tax liability was partially satisfied by such credits. As noted below, however, it is the Service's position that even if the overpayment credit is not needed for the estimated taxes for the

subsequent tax year, the latest date on which interest will begin to accrue on the subsequently determined deficiency for the first year will be the due date of the return, without extension, for the second year, in this case fiscal [REDACTED] ([REDACTED]).

In general the government is entitled to interest on a deficiency in tax for the period that the tax was due and unpaid. I.R.C. § 6601(a); Avon Products v. United States, 588 F.2d 342 (2d Cir. 1978). If a deficiency in tax is determined after the taxpayer elected to credit a return overpayment against its estimated tax liability for the next succeeding year, interest will begin to accrue on the amount of the deficiency equal to the amount of the return overpayment as of the effective date of the credit elect. H.R. Rep. No. 98-432 (Part II), 98<sup>th</sup> Cong., 2d Sess. 1489-1490 (1984), reprinted in 1984 U.S.C.C.A.N. 1132-1133; see also, Rev. Rul. 88-98, 1988-2 C.B. 356. Section 413 of the Tax Reform Act of 1984 provides that overpayments of tax will be credited against the estimated income tax for the next succeeding year with full regard to Rev. Rul. 77-475, 1977-2 C.B. 476.<sup>1</sup>

Rev. Rul. 77-475 provides the manner in which interest on a subsequently determined deficiency is computed under I.R.C. § 6601(a) when the taxpayer makes an election to apply an overpayment to the succeeding year's estimated taxes. When a taxpayer elects to apply an overpayment to the succeeding year's estimated taxes, the overpayment is applied to unpaid installments of estimated tax due on or after the date(s) the overpayment arose, in the order in which they are required to be paid to avoid an addition to tax for failure to pay estimated tax under I.R.C. § 6655 with respect to such year. However, in any case, the overpayment is a payment of the succeeding year's income tax liability no later than the due date (without regard to extensions) of the succeeding year's income tax return. Consequently, to the extent the overpayment is not needed to satisfy specific installments of estimated tax for the succeeding year's estimated tax, interest on the first year's deficiency begins to run from the original unextended due date of the succeeding year's income tax return.

In the instant case, the taxpayer's fiscal [REDACTED] ([REDACTED]) tax year does not fit within the fact pattern set forth in May Department Stores Co. v. United States, 96-2 U.S.T.C. ¶ 50,596

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<sup>1</sup> In 1983 the Service revoked Rev. Rul. 77-475. However, in response to tremendous public criticism and expected Congressional action, the Service promulgated Rev. Rul. 84-58, 1984-1 C.B. 2564, which reinstated and modified Rev. Rul. 77-475 on March 30, 1984.

(Fed. Cl, 1996) because it had fully paid all of its installments of estimated tax for fiscal [REDACTED] ( [REDACTED] ) and, therefore, did not need any of the return overpayment from fiscal [REDACTED] ( [REDACTED] ) to pay the estimated tax for fiscal [REDACTED]. The recent case of Sequa, supra, stands for the proposition that interest on the deficiency for the first year would not begin to run where there has been no application of the overpayment to pay estimated taxes of subsequent tax years in order to avoid the addition to tax for failure to pay estimated taxes under I.R.C. § 6655, or the overpayment has not been refunded. Accordingly, the taxpayer in this case can argue, relying on the rationale of Sequa, that the Service has had the benefit of the fiscal [REDACTED] ( [REDACTED] ) overpayment from the time it was generated in fiscal [REDACTED] and interest will not begin to accrue on the subsequently determined deficiency for the year until such time as the overpayment is used by the taxpayer to pay estimated taxes in order to avoid the addition to tax for failure to pay estimated taxes under section 6655, which in this case is beyond the end of the fiscal [REDACTED] ( [REDACTED] ) year. However, as noted above, the Service disagrees with the Sequa decision and has taken the position that in all cases, the overpayment is a payment of the succeeding year's income tax liability no later than the due date (without regard to extensions) of the succeeding year's income tax return.

In summary, no part of the taxpayer's fiscal [REDACTED] ( [REDACTED] ) return overpayment was needed to avoid the addition to tax for failure to pay estimated income taxes in fiscal [REDACTED] ( [REDACTED] ). Therefore, interest on the subsequently determined deficiency for fiscal [REDACTED] ( [REDACTED] ) begins to run from the date on which the return overpayment is applied to the succeeding year's tax liability which will not be later than the unextended due date of the succeeding year's income tax return. In this instance the overpayment from fiscal [REDACTED] will be applied to the next year's liability on the unextended due date of the fiscal [REDACTED] ( [REDACTED] ) return and this date is [REDACTED]. Thus, interest on the deficiency for this taxpayer's fiscal [REDACTED] ( [REDACTED] ) deficiency will run from [REDACTED].

As no further action is required by this office we are closing our file. If you have any questions, contact the undersigned at (816)283-3046, ext. 164.

(Signed) Dale P. Kensinger

DALE P. KENSINGER  
Assistant District Counsel